

Housing Microfinance

Opportunities and Constraints

CMFR Seminar

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Why Housing?

Context

Internal
Constraints

External
Constraints

Product
Design

Conclusion

- “Roti, kapda aur makan”: housing is a basic need
- Unmet housing demand
- Improvement of housing = improvement of quality of life (health, morbidity and related costs)
 - Housing used as a measure of poverty
- Housing as a means to asset realization for borrowers; collateral leverage in mainstream finance
- The house is the locus of daily life, especially for women
- Housing generation/improvement as a pump-prime for employment and investment at the community level

Housing Needs of the Poor

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- Emergency/Disaster Response
- Infrastructure Additions
 - Water, electricity, sanitation
- Incremental Building
 - Repairs, additional room
- Kachha to Pukka
 - New housing construction

Origins of Housing Microfinance

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- Microcredit to Housing Finance (MFIs)
 - diversifying portfolio takes cue from microfinance model for small enterprises
- Shelter Advocacy to Housing Finance
 - NGOs that begin with advocacy and move to housing microfinance

→ Both of these recognize the need for financial services as an integral piece of housing improvement for the poor.

Why MFIs Introduce Housing Products

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- Portfolio diversification
 - Increase return on share capital, distribution of risk (with loan size and term), cross-subsidization opportunities
- Response to Competition
 - Promotion, differentiation, customer loyalty
- Disaster Relief
 - Housing often severely affected by natural disasters, opportunity for quick response
- Credit Plus
 - Promotes a particular social agenda

Housing Microfinance Products in India

Program	Loan Amount	Loan Term	Interest Rate		Collateral	Other
			Micro-enterprise	Housing		
Kalanjiam Foundation (DHAN)—New Construction / Upgrades	Rs. 20,000-45,000 / Rs. 3,000-15,000	Up to 12 years / Up to 7 years		12% / 18%	Unsecured, guarantee of 10% of loan amount	Administered through Federations' "housing cells"
SHARE Microfin—Upgrades	Rs. 10,000	Up to 1 year	15%	15%	Unsecured, group guarantee, completion of 3 loan cycles	Funded through ICICI Bank. Targets "star" borrowers.
SEWA Housing Loans—Paki Bhit	Up to Rs. 25,000	Up to 5 years	17%	14.5%/17%	Unsecured, 2 guarantors/ Secured with collateral	Financed by HUDCO and HDFC.
Kudumbashree — Bhavanashree	Up to Rs. 40,000	10-15 years		7.25%	Land and building; borrowers must have clear title deed and own >1.5 cents of land	Funded by State Bank of India, State Bank of Travancore, Canara Bank, Central Bank of India, Indian Bank, Indian Overseas Bank, Syndicate Bank, ICICI Bank, Union Bank of India...
Gram Vikas	Rs. 10,000 – 40,000	Avg. 15 years		9%		Loans accessed from HDFC. Gram Vikas offers technical training, bulk materials purchase, masons etc.

Where Loans for Housing and Microcredit Diverge

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First and foremost, housing loans are consumption loans

- Funding sources
 - Lack of dedicated credit lines for housing
 - Term risk
- Security Linkages
 - Larger, longer term loans necessitate credible security
- Lending methodologies
 - Group v. individual? Servicing through institutional finance or thrift cooperatives?
- Scale, capacity, sustainability!

End-Use Monitoring

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If a loan is dedicated to housing, shouldn't an MFI make sure it is used as effectively as possible?

- Construction services: ensuring durability
 - Who is doing the construction?
 - What materials are being utilized?
- Added costs related to end-use monitoring
 - Due diligence adds administrative costs
 - Is there a point at which the cost of end-use monitoring is not worth the added improvement/sustainability of housing?

The Existing Policy Environment: Land Title and Collateral

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- Traditional mortgages contingent on title deed
- Rural villagers often hold *de facto* or paralegal title to land
- No central housing registry in India
- Urban slum dwellers often renters, while landowners have no intention of upgrading shelter with their own resources

Subsidies and Grants

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Government subsidies/institutional grants crowd out opportunities for housing microfinance by:

- Capturing mindsets
- Creating a culture of expectation
- Fostering dependency on top-down solutions
- Inability to fill the gap between total housing need and subsidy/grants
- Funding dependent on budget cycle

→ This does not preclude the need for subsidies entirely! We will discuss later.

Other Supply Side Factors

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- Adequate construction materials
 - In terms of affordability and availability
- Adequate trained labor
 - Local labor supply
 - Traditional methodologies of construction limiting
- Engagement of housing industry
 - Little prior experience working with the poor
 - Beneficiaries not versed in managing contracts/workers

Product Development: Adapting to Constraints

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The case of Ankuram Sangamam Porum (ASP) in Andhra Pradesh.

- Started in July 2000
 - ASP lends to SHGs, only Dalits and mostly women: outreach over 100,000 members
 - ASP is not operationally self-sustainable
 - Funding comes from donor grants and term loans
 - Services include compulsory savings and life insurance, loans, and optional social security
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- Market assessment
 - Tailoring product
 - Identifying Partnerships

Assessment Methodology

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- Initial assessment of demand through a broad survey
- Region specific site visits
 - Interviews
 - Assessment of physical housing (conditions, costs, materials used, etc.)

Indicators of Demand

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1. Diversion of income generation loans for home improvements
2. No other forms of subsidies or credit for housing construction/improvement
3. Large loans available at higher interest rates
4. Presence of "housing emergencies" that necessitate large amounts to fix
5. Positive response at the mention of such loans
6. High annual costs of repairing repeated, faulty construction
7. Signs of insufficient financing (e.g. incomplete construction projects)

Ability to Repay

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Issues mirror those of traditional microcredit loans

- Irregular income and assessment of income from informal employment

However...

Proxies include

1. Diversion of income generation loans for home improvements
2. Ability to pay back similar loans that carry equal or higher interest rates
3. Income qualification, in certain instances
4. Home based businesses that would increase income if housing were improved

Market Segmentation

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Severely drought-prone area: **small loans** for basic improvements and basic infrastructure connections

Drought-prone area: **Medium-sized** loans to help avail government subsidy. A credit-cum-subsidy approach.



Fertile area: **Large loans, long loan** terms to build a concrete houses. Cost to build a house: ~1 lakh.

Linked Product: Risk Mitigation

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Most of ASP clients hold paralegal title, so security can be based on one or more of the following:

- Completion of n loan cycles
- A minimum savings amount
 - Savings is already compulsory
- Group guarantees
- First batch of housing finance loans serviced only to "A" rated MACS

Funding Sources

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For larger, longer term loans the following must be considered:

- Loans based on group savings will be too small, and interest will likely be high
- Housing portion of the portfolio will likely grow much faster and larger than the rest of the portfolio due to size and term of loans
- Short term loans will create term risk
- Dedicated funding for housing loans required—the trick is convincing lenders that even without collateral the risk is low!

Loan Terms

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- Determine Estimated Monthly Installments (EMI) through an affordability analysis
 - Based largely on income proxies
- **Loan term** based on affordability analysis and funding source
- **Amount of loan** based on affordability analysis coupled with need and loan term
- **The interest rate** can reflect the cost of funds and/or the institutional lending rate, however rates can be lowered through cross-subsidization for
 - Better marketing
 - Social benefit
 - As a reward for repeat borrowers

Added Features

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- Construction/technical assistance/end-use monitoring
 - Partnerships with NGOs
 - Fund through inflated interest
- Insurance
 - Ensures that investment is protected, particularly in disaster prone areas
 - Qualifying institutional lenders can offer packaged product

Partnerships

Context		Who	Why	Feasibility
Internal Constraints External Constraints Product Design	To build capacity	NGOs	<ul style="list-style-type: none"> • Technical expertise • Can bring own funding 	Very feasible given availability of NGOs with expertise.
Conclusion		Institutional Lenders	<ul style="list-style-type: none"> • Long term loans • Favorable rates 	Feasible with operations that meet assessment criteria. Meets priority lending requirement.
	To improve policy environment	Government	<ul style="list-style-type: none"> • To ensure subsidy goes to poorest of the poor • To implement credit-cum-subsidy scheme • To recognize paralegal title 	Can be messy. Some state governments notoriously bad at managing NGO relationships. Party politics get in the way.

Conclusion

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- Product development is about finding creative solutions to get around both internal and external constraints
- Housing microfinance loans that significantly differ from microcredit loans are not best suited for the poorest of the poor
- Partnerships provide the best means of fulfilling the multi-dimensional housing needs of the poor
- The potential of developing markets around housing for the poor is great; but unleashing capital markets is ultimately contingent on the policy environment